

FINANCIAL MANAGEMENT IN LOCAL GOVERNMENT: FREQUENTLY USED TERMS

Introduction

It is helpful to have a standard set of terms to describe common local government financial processes, fund accounts, and budgets. While there is a great deal of variation in the size, style and complexity of budgets prepared by our state's town, city, village and county governments, state reporting and accounting requirements have created more uniformity over recent years. Many of the following frequently used financial and budgeting terms are used regularly at all levels of local government. This glossary of terms should make what used to be a mysterious language clearer to all who are trying to understand and monitor local finances.

Glossary

Account

A classification established for the purpose of recording revenues and expenditures. (The various classifications used are likely to be drawn from a "chart of accounts" developed or adopted by the unit of government.)

Accounting basis

The method adopted for treating revenues and expenditures. The methods most likely to be found in use among small and medium-size units of government include:

The Accrual Basis of accounting under which revenues are recorded when earned (whether or not actual payment is received at that time) and expenditures are recorded when goods and services are received (whether or not payment is made at that time).

The Cash Basis of accounting under which revenues are recorded when received in cash and expenditures are recorded when payment is made in cash.

The Modified Accrual Basis under which (most kinds of) revenues are recorded when received in cash, but (most kinds of) expenditures are recorded when goods and services are received.

Activity

A specific, identifiable unit of work or service performed.

Appropriation

A legal authorization granted by the governing body which permits public officials to incur obligations and make expenditures up to the amount of money allocated and within time limits set by the governing body.

Audit	A careful examination, using generally accepted accounting principles and practices, giving the independent auditor's opinion whether or not revenues are fairly reported and whether expenditures are fairly reported.
Budget	<p>The managerial and political document in which the costs associated with various activities are estimated, anticipated revenues projected, and decisions made which result in appropriations, tax levies and borrowing authority.</p> <p>Also a plan forecasting the amounts of money to be expended, revenues and their sources. Two kinds of budgets are commonly used:</p> <p>The Operating Budget is the plan for current or annual expenditures and the proposed means of financing them.</p> <p>The Capital Budget is the financial plan that details expenditures for (many kinds of) equipment, repair projects, the purchase or construction of buildings and facilities, and the means of financing each over longer periods of time.</p> <p>(Also see "Performance budget", "Program budget" and "Zero based budget".)</p>
Budget calendar	The schedule of events that need to occur and the date or period of time for each to occur in the preparation, review and adoption of a budget.
Capital assets	Buildings, machinery, equipment or other items having a useful life of several years and/or costing a significant amount of money to acquire. (Also called fixed assets. Local policy determines the criteria for treating proposed budget items as capital assets.)
Capital improvement plan	A plan listing priorities for major capital improvement projects anticipated over a fixed number of years, their costs, and methods of financing the expenditures. (Among small to medium size units of government, a capital improvement program will typically span three to seven years.)
Capital outlay	Expenditures for the acquisition of new or replacement of current capital assets.
Cash flow plan	A projection of the cash receipts and disbursements anticipated during each week or month of the fiscal year. Usually requiring a cooperative effort by the clerk and treasurer, the plan helps determine the most opportune time to expend funds, helps avoid unnecessary short term borrowing, and earns the highest return on idle funds.
Debt service	The amount of money a unit of government must spend to repay in full and on schedule the principal and the interest owed on what it borrows from outside lenders.
Depreciation	That portion of the total expended to acquire a capital asset charged as an expense during a particular period of time. Depreciation is usually estimated in a straight line calculation in which the original value is

decreased each year as a percentage of full value over the expected life of the asset.

Encumbrance

Commitments to pay for equipment, goods or services without payment actually being made. Purchase orders and contracts are typical ways in which government agencies encumber funds charged against an appropriation for contracts yet to be performed.

Enterprise fund

An accounting method for revenues and expenditures of an activity that is treated much like a business enterprise because it is expected to be self supporting, with little or no subsidy provided from general funds, and with an ongoing independent revenue source.

Fixed assets

See “Capital assets”.

Fund

An independent accounting entity with its own set of accounts to record revenues and expenditures, obligations, and reserves. (Most local units of government establish a general fund along with several special revenue funds and, if appropriate, enterprise funds.)

General reserves

Revenues received but not needed until a future date in order to meet obligations; these revenues can be invested in a variety of authorized ways to generate additional income. (The investment of idle funds requires coordination between cash flow planning and budget planning.)

Liquidity

The ability to convert an investment (of idle funds) quickly in order to meet obligations with minimum loss of earning power.

Line-item/object-of-expenditure budget

The classification of expenditures on the basis of categories called objects-of-expenditure (personal services, contractual services, capital outlay, etc.) and within each category more detailed line-items (salaries, travel, telephone expense, etc.). (This type of budget, traditionally used among local units of government, focuses attention on how much money is spent and for what purpose rather than the activity affected or its outcomes.)

Management letter

A letter from the independent auditors that is usually a series of findings or recommendations on ways the financial management policies and practices may be improved.

Performance budget

The classification of expenditures on the basis of specific activities (resurfacing streets, investigating traffic accidents, etc.), the number of units performed and their costs. (This type of budget focuses attention on what a work unit does, how frequently it does it, and at what cost rather than a detailed, line-item accounting of expenditures.)

Program

Group activities, operations, or organizational units directed to attaining specific purposes or results. (A group of activities related to crime prevention can be made part of the same program even though the activities involve separate work units within the same program under the same governing body. The same may be true of activities related to fire prevention, health care centers, road maintenance, etc.)

Program budget	The classification of expenditures on the basis of programs, significant problems or policy issues each attempts to deal with, and alternatives for dealing with them. (This type of budget focuses attention on the kinds of problems and policy issues chief executives and governing bodies are expected to resolve and, in a summary fashion, the resources needed to resolve them.)
Restricted assets	An account set up to control monies or other resources, the use of which is restricted by legal or contractual requirements.
Reserve for contingencies	An account, included as part of most budgets, set aside for emergencies or other unanticipated needs not otherwise included as part of a budget. (Since a contingency fund is usually included in the adopted budget, it takes a simple majority of the governing body to approve spending from it.)
Transfer of funds	An approved movement of monies from one separate fund to another fund. Often budgets call for Transfers In to the General Fund to pay for centralized expenditures such as utilities, insurance, or fringe benefits. Transfers Out from the General Fund may be required to subsidize new special activity funds or those with insufficient or unreliable revenue sources.
Unreserved fund balance	Available funds from prior year budgets that the local government's auditors have determined are not pledged for any purpose that may be used as a guarantee for the credit of the government's long term bonds, or for any legal general purpose. (Unreserved funds are considered outside the normal operating budget unless applied as "Funds Forwarded" to reduce the tax levy. Expenditure of these funds requires a 2/3 vote.)
Zero-base budget	A budgeting approach whereby the expenditure amount for each line item is examined in its entirety each year, regardless of prior funding. Those items that cannot be justified are subject to elimination.

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